Introduction to International Business

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Aims

- Explore some of the key issues and themes from the business perspective,
- Including how multinational corporations deal when seeking to exploit international business opportunities,
- The management challenges presented.
- Using frameworks and methodologies, students will investigate the interaction between firm strategies, economic policies, and the changing international environment.

Learning Outcomes

- To gain an understanding of the international business environment and its competitive and investment climate
- To provide students with an in-depth understanding of the correlations between international and the global economy
- To examine issues from both a business and economic perspective
- To enhance your understanding of the strategic context in which international business operates
- To help prepare you for a career in large multinational corporations.

Topics for Week 2

1. Introduction to International Business
2. The International Economic Environment
3. Multinational Corporations: internal organization and strategies
4. Market Structure and Firms' Strategies
5. Business Strategy - Use of Game Theory

Suggested Reading

- Simon Collinson, Rajneesh Narula, Alan M. Rugman and Amir Qamar, International Business, 8th Edition, Pearson Education, 2020
- John Lipczynski, John Goddard and John O.S. Wilson, Industrial Organization: Competition, Strategy and Policy, 5th Edition, Pearson Education, 2017
- Sloman, John, et al. Economics for Business Enhanced. Available from: VitalSource Bookshelf, (8th Edition). Pearson International Content, 2019.

Introduction Lecture outline

- What is international business?
- Globalization
- Socio-political developments
- What are institutions?
- Multinational enterprises
- Foreign direct investment
- International business in the modern era
- Outsourcing, offshoring and nearshoring

What is international business?

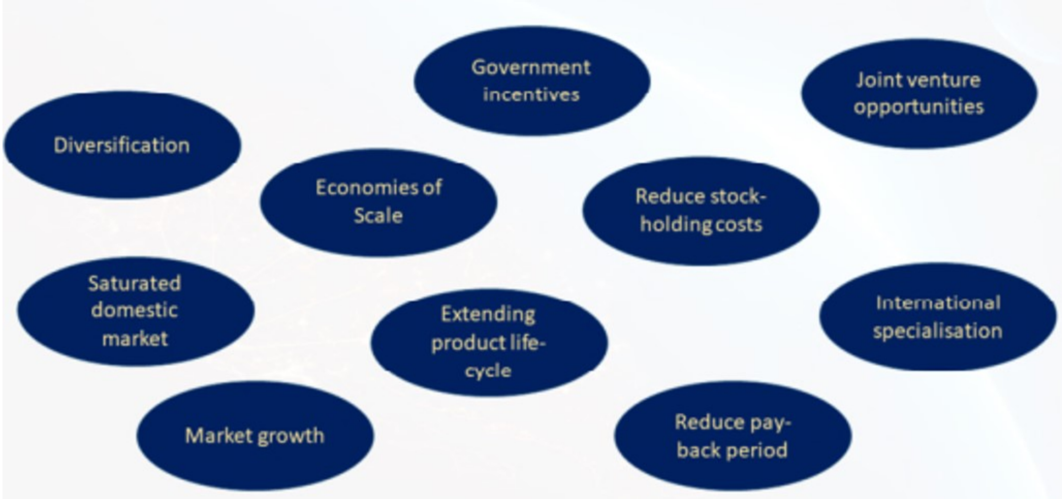
- **International business:** The study of transactions taking place across national borders for the purpose of satisfying the needs of individuals and organizations.
- The '**classical**' view of international business has been international trade, in the form of exporting and importing.
- International firms are responsible for about **one-third of global trade,** much of which moves between affiliates: that is, these goods and services are being exchanged across borders but within the same MNE.

Reasons to internationalize?

Can you name any?

Passcode: 2024

Reasons to internationalize

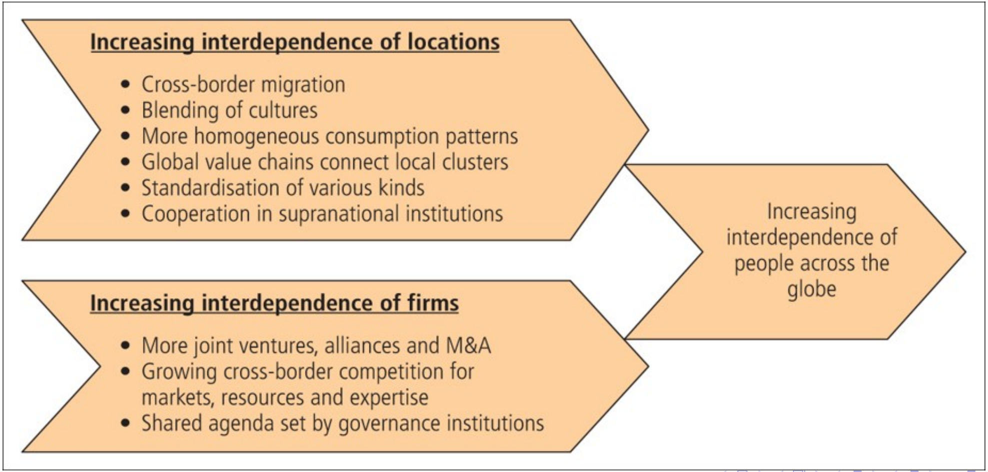


Globalization

- Globalization, however, remains a vague concept, used by different people in different ways.
- **Economic Globalization:** The growing interdependence of locations and economic actors across countries and regions.
- Do not seek to take sides in the debate about the pros and cons of globalization, or to engage in a discussion of '**making globalization good**'.
- It is simply a fact of the twenty-first century, and it is an ongoing process, rather than an event.
- Not used the term 'global firm', but instead we refer to 'international firms' or '**multinational enterprises**'.
- There is a tendency to mistake internationalisation for globalisation, and the key to differentiating the two is the issue of **interdependence**.

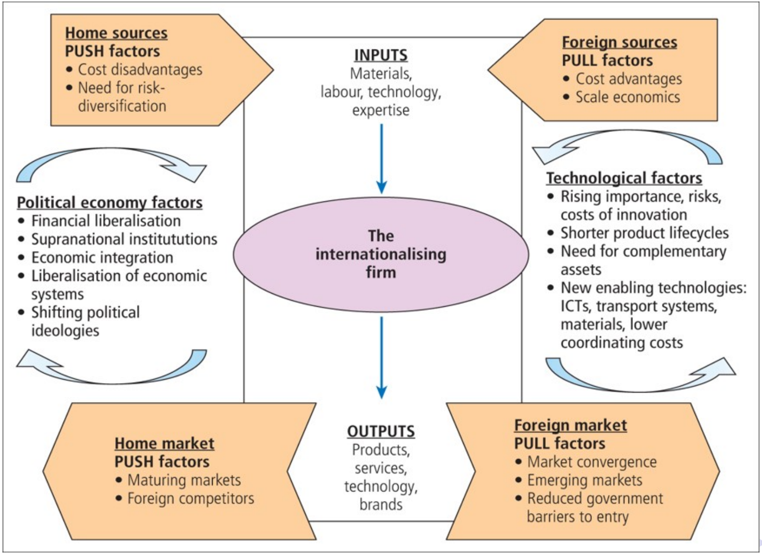
Globalization

- **Interdependence** is the essence of globalization, and as usual, it is a continuum, with firms, individuals and countries demonstrating different degrees of interdependence.
- **Consequences of Globalization:**



Globalization (Continued): The dynamics of globalization

- Interdependence: Internationalization vs Globalization.
- Mapping Globalization can be a difficult task.
- Driving Forces:



Socio-political developments

Economic interdependence is partly driven by political events, and most importantly by political stability. Stability of policies, and the creation and maintenance of the appropriate environment, plays a significant role in promoting the appropriate environment for firms to prosper.

- First, firms and entrepreneurs need to be able to claim and defend their **property rights**.
- Second, they need to be able to **establish contracts that are legally enforceable**, and to be able to do so at a reasonable cost and within a reasonable timeframe.
- The **World Bank's Doing Business** survey estimates the average time it takes to enforce a contract through the law courts, and it is easy to see the considerable differences between countries.
- Eg: A Dutch firm undertaking a joint venture with a Brazilian company would typically sign three contracts: one under Dutch law, another under Brazilian law, and a third contract under US law, so that disputes could be managed by referring to the English text. This creates costs for both firms, since each needs to retain three legal teams in three different countries.

What are institutions?

- **Institutions**: "Sets of common habits, routines, established practices, rules, or laws that regulate the interaction between individuals and groups."
- **Formal**: Rules that can be of the form of legal codes and laws. Can exist within a firm such as responsibilities, job descriptions, codes of conduct, and accounting and financial regulations. (E.g. GATT, WTO)
- **Informal**: Are not always laid out in the form of written instruction, but come out of usage and tradition and are often unwritten and tacit.

- **GATT**: Established in 1947 to liberalize trade and to negotiate trade concessions among member countries. Today, the WTO is enforcing the provisions of the GATT.
- **WTO**: Established on January 1, 1995. An international organization that deals with the rules of trade among member countries. Enforces the provisions of the General Agreement on Tariffs and Trade (GATT). Acts as a dispute-settlement mechanism.

Multinational enterprises

- **Multinational enterprises (MNE)**: "A firm that engages in value-added international business activities, that has affiliates in more than one country, and whose operations and activities in different locations are actively coordinated by one or more headquarters organizations."

- The use of the term 'MNE' as a synonym for FDI is increasingly inaccurate. MNEs can and do organise activities through global production networks (GPNs) and global value chains (GVCs), and manage ongoing and systematic vertical transactions through multiple headquarters, which may or may not be associated with a singular 'parent company'.

- The MNE has traditionally also been regarded as having a **distinct 'home country' where its headquarters are located**, and which acts as the command centre, providing primary strategic direction for its affiliates in various 'host countries', as well as providing the primary or core assets on which the affiliates base their operations.

- Indeed, **the home country establishment is referred to as the 'parent firm'**, implying that the home country is at the top of a hierarchy of affiliates or subsidiaries. Furthermore, residents of the home country are assumed to own (and therefore control) the international operations of the MNE.

Misconceptions about MNEs

Common misconceptions about MNEs:

- MNEs have far-flung operations or **earn most of their revenues overseas**.
- MNEs are globally monolithic and excessively powerful in political terms.
- MNEs produce **homogeneous products for the world market** and through their efficient techniques are able to dominate local markets everywhere.

Misconceptions about MNEs (Continued)

- Despite the importance given to MNEs, they do not account for a dominant or even a major share of the world's economic activity.
- In terms of employment, the world's largest MNEs employed 75 million directly in 2014, up from about 20 million in 2000. Despite this steady increase, MNCs account for **only 2 per cent of global employment** (as of 2017).
- MNEs **earn most of their revenues in their home regions**.
- The largest 500 MNEs are not spread around the world but are clustered around the triad.
- These MNEs engage not in global competition but in triad/regional competition; this rivalry effectively eliminates enduring political advantage.
- MNEs **adapt their products for the local market**.
- Majority of MNEs come from developed-economy home countries.

MNE activity

Most MNE activity can be classified into two major categories:

1. **Trade (exports and imports)**: Approximately more than 50 percent of all trade is made by the world's largest 500 MNEs.
2. **Foreign direct investment (FDI)**: Approximately 80 percent of all FDI is made by the world's largest 500 MNEs.

Foreign direct investment (FDI) is equity funds invested in other nations.

- **Inward FDI flows** are money coming into a country during the reporting year, from foreign-owned MNEs to their subsidiaries in country A. In this case, country A is known as the host country.
- **Outward FDI flows** are money going out, from firms that are registered in country A (known as the home country) to their subsidiaries in other countries.

Foreign investment (FI)

- **Foreign Direct Investment (FDI)**: Involves acquiring a significant degree of influence and control over a foreign business entity. This typically means owning 10% or more of the foreign company's shares or equivalent equity.
  - **Greenfield Investment**: Establishing new operations or facilities from scratch in a foreign country.
  - **Brownfield Investment**: Acquiring or merging with an existing foreign business.
- **Foreign Portfolio Investment (FPI)**: Involves purchasing financial assets such as stocks, bonds, or other financial instruments in a foreign country without seeking control or significant influence over the entities issuing these securities.

The World's Top Recipients of Foreign Direct Investment?

https://www.imf.org/en/Blogs/Articles/2021/12/16/the-worlds-top-recipients-of-foreign-direct-investment

International business in the modern era

The international business environment has changed rapidly in recent years as a result of:

- an overall slowdown of triad economies;
- increased trade liberalization through trade agreements;
- improvements in technology;
- the emergence of SMEs.

International business in the modern era (Continued)

- Much of the growth in new MNEs from emerging markets reflects the growth of China. However, the number of Chinese firms entering the Global Fortune 500 tripled between 2010 and 2014 years, the evidence suggests that few of them are truly internationalized.
- Although there is considerable hype about the growth of emerging country MNEs (EMNEs), the hard evidence is less impressive. Not all foreign investment is necessarily a foreign direct investment.
- Investments from developing countries may represent an institutional investment through a private equity firm, a sovereign wealth fund, or a portfolio investment.
- This is the case in many of the acquisitions by oil-exporting countries (including the Middle East countries, but also Russia) and China, where individuals or (state-owned or state-influenced) firms have access to capital, and acquire ownership in companies.

Outsourcing, offshoring and nearshoring

- From the 1990s, there was also a relocation of labour-intensive industry functions from rich countries to lower-wage countries with skilled workforces. This followed a new tendency to 'fine-slice' activities so that they could be modularised, thereby taking advantage of cheaper inputs wherever they might be. Back-office processing, call centres, accounting and software maintenance and development all became growth industries for countries such as India, the Philippines, Egypt, Mauritius, Pakistan, South Africa and others.

The rapid growth and popularity of global networks and global value chains is linked to the phenomena of outsourcing and offshoring.

- Traditionally, **outsourcing** was done by manufacturing firms that, rather than having a fully vertically integrated supply chain, *would have some or all of the parts and components of their products manufactured by someone else and do the assembly of the final product themselves*.
- Eg. Toyota produces less than 30 per cent of the value of cars that roll off its assembly lines the remaining 70 per cent comes from independent suppliers.

Outsourcing, offshoring and nearshoring (Continued)

- When the outsourcing is done to a location beyond the national borders it is called **offshoring**.
- Offshoring can be done internally by moving activities from a parent company to its foreign affiliates (sometimes referred to as captive offshoring, involving FDI), or outsourced to third parties offshore in other countries.

Decisions over offshoring are largely **driven by**:

- differences in production cost,
- taking into consideration transportation costs for both inputs and outputs,
- and the need to coordinate between units based in different locations.

Outsourcing, offshoring and nearshoring (Continued)

In recent years we have witnessed an increasing trend in nearshoring. The concept of **nearshoring** refers to relocation (offshoring) to a nearby country. Some of the driving forces behind the rise of nearshoring include:

- lower transportation costs;
- smaller time zone differences;
- time-to-market; and
- lesser liability of foreignness.